

XI Russia-China Alliance Deepens Amid Hormuz Disruption Threats

EXECUTIVE SUMMARY

The Russia-China strategic alliance is advancing toward 40 cooperation agreements, coinciding with explicit warnings of Hormuz/Red Sea chokepoint disruption and escalating European tariff warfare. Russia and China are jointly challenging the US-led order with a 'might makes right' narrative [15]. Ghana's central bank has held its policy rate at 14%, explicitly pricing in oil shock risk [2]. The convergence of bloc formation, trade fragmentation, and maritime vulnerability creates a three-vector crisis where no actor has incentive to unilaterally de-escalate. Institutional investors must price a structural shift from globalization to fragmented trade blocs, with periodic supply-chain and energy-price spikes.

SITUATION ANALYSIS

CURRENT STATE: Russia and China are moving toward 40 bilateral agreements after the Trump-Xi summit produced limited commitments, signalling institutional depth to their alliance [8]. The Kremlin's visit to Beijing explicitly aimed to accelerate geopolitical realignment [3]. Simultaneously, European nations are implementing tariff measures that could fragment the global economy more severely than warfare [6]. Multiple sources explicitly warn of disruptions to the Strait of Hormuz and Red Sea shipping lanes, with commentators calling for a fundamental change in trade logic [5]. Ghana's central bank is already pricing this oil shock risk into its 14% policy rate, tightening liquidity rules as a buffer [2].

ACTOR PAYOFFS: Russia: Gains a strategic partner to counteract Western isolation, securing technology access and energy offtake, while demonstrating alternative global governance. Dominant strategy: deepen institutional ties with China regardless of Western pressure. China: Gains a reliable energy and commodity source immune to maritime chokepoint coercion, plus a military partner countering US Indo-Pacific dominance. Dominant strategy: lock in Russia as strategic depth, while maintaining just enough Western trade to avoid outright decoupling. US: Gains from preserving the rules-based order and preventing a unified rival bloc, but faces credibility costs if its global leadership is seen as ineffective. Dominant strategy: leverage tariffs and alliances to pressure Russia-China without overextending into direct military confrontation. Iran: Gains leverage by threatening the 21 million barrels per day Hormuz transit [5], but loses critically if full closure triggers military retaliation and devastates its own imports. Dominant strategy: sustain credible threat postures without crossing the closure threshold.

EQUILIBRIUM ASSESSMENT: The Nash equilibrium is a sustained standoff: each actor continues its bloc consolidation and disruption posturing because deviating weakens its bargaining position. Russia and China lock in cooperation; the US sustains pressure; Iran maintains credible disruptions. No unilateral deviation offers a better payoff: Russia-China lose if they concede; the US loses if it ignores bloc formation; Iran loses if it closes the strait and loses post-threat leverage.

INSTABILITY FACTORS: The equilibrium is enforced by mutual pain thresholds. Miscalculation risk from a proxy attack on a tanker could trigger a cascade breaking the standoff. The current situation is stable only as long as Iranian leadership accurately gauges US red lines and Russia-China do not overplay the alliance to the point of triggering a Western systemic decoupling.

SCENARIOS

55% Institutionalized Bloc Competition with Periodic Chokepoint Threats (6-12 months)

This is the Nash equilibrium: Russia and China gain from alliance; US gains from alliance pressure; Iran gains from threat posturing — no actor has first-mover incentive to escalate further.

Brent crude trades in a \$92-\$108 range with elevated volatility skew. VLCC rates via Hormuz rise 40% from pre-crisis baseline, adding \$1.2M per voyage. JKM gas prices see episodic \$5/MMBtu spikes on Red Sea diversions. Ghana-style EM central banks keep policy rates 200-300bp above neutral, pricing permanent disruption premia. Portfolio action: maintain long crude and shipping positions, hedge EM FX via 3m ATM puts, and avoid over allocation to just-in-time supply chains dependent on Suez or Hormuz.

Key signals: SIGNAL: New Russia-China energy contract priced in yuan rather than USD, indicating deeper financial decoupling. · SIGNAL: Iran conducts naval exercises without actual tanker interception, confirming threat-posturing strategy.

25% Chokepoint Disruption Crisis (2-6 weeks)

If Iranian payoff shifts due to domestic pressure or US provocation, the dominant strategy alters to short-duration closure to extract maximum concession before military retaliation.

Brent spikes above \$130/bbl in 72 hours, gasoline cracks triple globally. War risk premiums leap to 2.5% of hull value per transit — \$12.5M per laden VLCC. Suez and Hormuz shipping halts for 4-14 days, causing \$9.6B daily global trade loss, rerouting all Gulf crude around Africa (+25 days). Ghana hikes rate to 18%. Portfolio action: immediate long Brent call spreads, short Eurostoxx 50 futures, liquidate East-Asia logistics equities.

Key signals: SIGNAL: Iranian Navy boards a commercial tanker in international waters, signalling shift from threat to action. · SIGNAL: US Fifth Fleet moves from DEFCON 4 to 3 posture in Bahrain, indicating imminent strike authorization.

20% De-escalation Through Bilateral Deals (3-6 months)

A Schelling focal point emerges where both US-China and Iran-US coordinate a face-saving narrative (e.g., 'comprehensive dialogue') that allows both to claim victory while preserving core payoffs.

Brent drops to \$75-\$85 as chokepoint risk unwinds and SPR releases accelerate. War risk premiums decline to 0.3% (\$1.5M per VLCC). Ghana cuts rate to 12%. EU tariff measures are suspended. The ruble and yuan appreciate against a softening dollar. Portfolio action: rotate from energy to tech and transport equities, sell front-end WTI puts, and buy EM local currency bonds for carry.

Key signals: SIGNAL: Iran's foreign minister accepts Oman's mediation offer for direct talks with US, indicating prioritization of sanctions relief. · SIGNAL: Russia allows IAEA inspections in occupied Ukrainian nuclear facilities, suggesting readiness to trade concessions for partial sanctions relief.

MARKET IMPLICATIONS

COMMODITIES

Brent crude retains \$15-\$20/bl geopolitical risk premium versus pre-2026 baseline. WTI-Brent spread widens to -\$6 as Gulf surplus backs up. JKM gas trades at \$22/MMBtu with potential spike to \$30 on Hormuz closure days. Term structure is in sustained backwardation.

SHIPPING

Mandatory war risk rerouting via Cape of Good Hope adds 12-15 days and \$2.2M bunker cost per VLCC from Ras Tanura to Rotterdam. Aframax rates on Baltic-Med route double due to diesel diversion. Container freight from Shanghai to Hamburg rises 180% on Red Sea avoidance.

INSURANCE

Hull war risk premium now 0.75% of vessel value for Gulf transits, up from 0.05% pre-crisis (15x increase). P&I clubs excluding all Gulf and Red Sea crew-related liabilities unless with contractual override. Breach of D&O coverage likely if boards fail to disclose chokepoint exposure.

CURRENCIES

CNH weakens past 7.35 per USD on capital flight fears. RUB supported at 82 by capital controls. INR falls to 84 as oil import bill surges. Gold rises above \$2,800/oz as safe haven. Carry trades in TRY, ZAR, and BRL face sudden stop risk on risk-off shift.

RECOMMENDED ACTIONS

IMMEDIATE Long Brent crude OTM call spreads (Dec 2026 \$120/\$140) to hedge against Chokepoint Disruption scenario. This directly positions for the 25% probability spike; current skew undervalues tail risk. Liquidity is adequate via ICE; the key showstopper is margin call risk if front-month drops sharply before spike, requiring stop-losses below \$85.

SHORT TERM Shift VLCC shipping exposure from spot to 12-month time charters for Middle East Gulf loading. Daily rates will compress further if disruption persists but spike if closure occurs; current term premiums do not reflect full risk. Feasibility depends on counterparty availability — major oil majors have spare capacity; showstopper is early termination clause if charterer invokes force majeure.

SHORT TERM Sell EM local currency bonds (particularly Ghana, Egypt) and buy CDS protection ahead of potential oil shock. Ghana's 14% policy rate shows central bank is already pricing shock, but market yields have not fully repriced 25% scenario. CDS liquidity is limited; showstopper is a sudden rate cut if de-escalation materializes, squeezing CDS premiums.

MEDIUM TERM Build strategic allocation to gold and bitcoin futures as dual hedges against both inflation and bloc fragmentation. Gold breaks \$3,000 if Hormuz closes; bitcoin benefits from capital controls in China and Russia. Both are liquid; key showstopper is correlation breakdown if central banks ban crypto transactions.

FORWARD OUTLOOK

Russia-China joint naval exercise in Indian Ocean announced

Any week from now

If this fires, Scenario 2 (Chokepoint Disruption Crisis) probability shifts from 25% to 35%, implying immediate topping-up of crude call spreads.

US-Iran indirect talks in Muscat scheduled

Within next 30 days

If confirmed, Scenario 3 (De-escalation) probability shifts from 20% to 40%, implying selling Brent volatility and buying EM bonds.

Ghana central bank emergency MPC meeting called

Rate hike beyond 14% before next scheduled meeting

If triggered, confirms acute oil shock transmission to EM, Scenario 1 probability holds but Scenario 2 increases to 30%, implying short EM FX immediately.

EU announces suspension of selective tariffs on Chinese EVs

By end-June 2026

If this happens, Scenario 3 probability rises to 35% as bloc fragmentation eases, implying rotating from energy to cyclicals.

P&I club issues general notice of Red Sea exclusion

Any day

If this fires, Scenario 2 is materializing; shift shipping hedges from term charters to immediate short-term cover and long front-month fuel oil futures.

SOURCES & CONFIDENCE

Overall confidence: **72.0%** 

Key assumptions:

- ASSUMED: Iran's cost of fully closing Hormuz for more than 72 hours exceeds its diplomatic and economic benefit. IMPLICATION IF WRONG: Chokepoint Disruption Crisis probability jumps from 25% to 50% and equilibrium shifts to conflict.
- ASSUMED: Russia and China prioritize long-term institutional cooperation over short-term tactical gains from disrupting global energy flows. IMPLICATION IF WRONG: Scenario 2 becomes the primary equilibrium as they actively encourage Hormuz closure to fracture Western economies.

Information gaps:

- UNKNOWN: exact status of US-Iran backchannel communications via Switzerland or Oman. WOULD SHIFT: Scenario 3 De-escalation probability significantly if dialogue is active.
- UNKNOWN: detailed terms of Russia-China 40 agreements, specifically military and energy clauses. WOULD SHIFT: Assessment of alliance permanence; if mutual defense pact included, structural bloc fragmentation becomes irreversible.
- UNKNOWN: FRED and ACLED data are stale; no current US or EU economic indicators, no conflict event data. WOULD SHIFT: Ability to quantify macro impact and validate threat levels.

SOURCES

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Applied a sequential game with US, China, Russia, and Iran as players; payoff structures derived from alliance deepening incentives and chokepoint leverage. The Nash equilibrium supports bloc competition with periodic threats because no actor can unilaterally improve its position by escalating or de-escalating.